

Audit



Report

OFFICE OF THE INSPECTOR GENERAL

**DOD MILITARY RETIREMENT TRUST FUND
FINANCIAL STATEMENTS FOR FY 1992**

Report No. 93-136

June 30, 1993

DISTRIBUTION STATEMENT A
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Acronyms

| | |
|------------|---|
| ASD (FM&P) | Assistant Secretary of Defense (Force Management and Personnel) |
| DFAS | Defense Finance and Accounting Service |
| DMDC | Defense Manpower Data Center |
| DoL | Department of Labor |
| FMFIA | Federal Managers' Financial Integrity Act |
| GAO | General Accounting Office |
| OMB | Office of Management and Budget |
| P.L. | Public Law |



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202

June 30, 1993

MEMORANDUM FOR SECRETARY OF DEFENSE
COMPTROLLER AND CHIEF FINANCIAL OFFICER,
DOD

SUBJECT: Audit Report on the DoD Military Retirement Trust Fund Financial
Statements for FY 1992 (Report No. 93-136)

We are providing this report for your information and use and for use by Congress. Financial statement audits are required by the Chief Financial Officers Act of 1990 (the CFO Act). Office of Management and Budget (OMB) Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993, which implements the CFO Act, requires the Inspector General to render an opinion on the fairness of the financial statements. We are also required to report on the adequacy of internal controls and compliance with laws and regulations.

Part I contains our unqualified opinion on the DoD Military Retirement Trust Fund Financial Statements for FY 1992. The Principal Statements and the Notes to the Principal Statements present fairly, in all material respects, the assets, liabilities, and net financial position of the DoD Military Retirement Trust Fund as of September 30, 1992, and the results of its operations, cash flows, and reconciliation for the year then ended, in accordance with DoD accounting policies and procedures and generally accepted accounting principles.

In Part II, we report that the DoD Military Retirement Trust Fund was administered with adequate internal controls to ensure that the financial statements were free of material error. At three Defense Finance and Accounting Service Centers (DFAS Centers), however, we found a lapse in controls that required disclosure.

In Part III, we report that except for the following noncompliances, the DoD Military Retirement Trust Fund was administered in compliance with laws and regulations. We found that the DFAS Centers did not consistently and properly assess interest, penalties, and administrative charges on retirees' debts. Further, the DFAS Centers did not effectively use all debt collection techniques available to them. The DFAS-Denver Center also did not implement Public Law 98-94, which required the rounding down of retiree entitlements, in a timely manner. We also noted deficiencies in the statements that were required by OMB Bulletin No. 93-02; however, these deficiencies did not affect our overall opinion on the financial statements.

This report contains no recommendations that are subject to resolution in accordance with DoD Directive 7650.3; therefore, comments are not required. If you have any questions about this audit, please contact Mr. Raymond D. Kidd, Program Director, at (703) 614-1682 (DSN 224-1682), or Mr. John M. Seeba, Project Manager, at (703) 693-0653 (DSN 223-0653). The courtesies extended to the audit staff are appreciated. The distribution of this report is listed in Part IV, Appendix C.

A handwritten signature in black ink, reading "Robert J. Lieberman". The signature is fluid and cursive, with the first letters of the first and last names being capitalized and prominent.

Robert J. Lieberman
Assistant Inspector General
for Auditing

Office of the Inspector General, Department of Defense

Audit Report No. 93-136
(Project No. 2FH-2014)

June 30, 1993

**AUDIT REPORT ON THE DOD MILITARY RETIREMENT TRUST
FUND FINANCIAL STATEMENTS FOR FY 1992**

EXECUTIVE SUMMARY

Introduction. The Chief Financial Officers Act requires an annual audit of funds such as the DoD Military Retirement Trust Fund (the Fund). The Fund was established in 1984 by Public Law (P.L.) 98-94 to provide retirement benefits for military personnel and their survivors. For FY 1992, the Fund paid \$24.6 billion to 1.5 million retirees and 181,000 survivors. As of September 30, 1992, the Fund's assets were \$106.1 billion and its unfunded liability was \$411.9 billion. The Fund received revenue from three sources during FY 1992: contributions from the Services (\$16.3 billion), payments from the U.S. Treasury for the unfunded liability (\$11.2 billion), and interest earned on U.S. Treasury securities (\$9.4 billion). As of May 1993, a Fund manager had not been named. The Assistant Secretary of Defense (Force Management and Personnel) has been recommended to the Deputy Secretary of Defense for designation as the Fund manager; however, no official appointment had been made.

Objectives. The objectives of the audit were:

- o to determine whether the DoD Military Retirement Trust Fund financial statements for FY 1992 were fairly presented, in accordance with DoD accounting policies and procedures and generally accepted accounting principles,
- o to determine whether there were adequate internal controls over the Fund to ensure that the financial statements were free of material error,
- o to assess compliance with laws and regulations for transactions and events that have a direct and material effect on the financial statements, and
- o to determine the reliability and usefulness of the financial statements.

Independent Auditor's Opinion. In our opinion, the Principal Statements and the Notes to the Principal Statements present fairly, in all material respects, the assets, liabilities, and net financial position of the DoD Military Retirement Trust Fund as of September 30, 1992, and the results of its operations, cash flows, and reconciliation to budget for the year then ended, in accordance with DoD accounting policies and procedures and generally accepted accounting principles.

Internal Controls. Our review of internal controls for the Fund did not disclose any material internal control weaknesses as defined in P.L. 97-255, "Federal Managers' Financial Integrity Act of 1982," Office of Management and Budget (OMB) Circular No. A-123, and DoD Directive 5010.38. We also did not identify any weaknesses that

we consider to be reportable under standards established by OMB Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993.

Compliance with Laws and Regulations. We noted that the DFAS Centers (the Centers) did not fully comply with the Debt Collection Act of 1982, P.L. 97-365. The Centers did not consistently and properly assess interest, penalties, and administrative charges on debts due from retirees. This area of noncompliance has been an ongoing problem for managers at the Centers. The General Accounting Office, the Service audit organizations, and the IG, DoD, have documented the Debt Collection Act of 1982 as an area of noncompliance for the past 5 years. Noncompliance with laws and regulations could also represent internal control weaknesses; however, we defined the problem as noncompliance with laws and regulations.

The DFAS-Denver Center did not implement P.L. 98-94, which required the rounding down of retiree entitlements, in a timely manner. We also noted deficiencies in the statements that were required by OMB Bulletin No. 93-02; however, these deficiencies did not affect our overall opinion on the financial statements. Except for noncompliances with the Debt Collection Act of 1982, P.L. 97-365, and the Defense Appropriations Act, P.L. 98-94, we believe that the DoD Military Retirement Trust Fund complied in all material respects with applicable laws and regulations.

Usefulness of Financial Statements. We found the financial information to be reliable and useful for users who need it for purposes such as budgeting. However, we did not identify any managers or organizations that use the financial statements. We believe that the usefulness of the financial statements decreases when they are issued 6 months or more after the end of the reporting period.

Management Comments. We provided draft reports of Parts II and III to management on May 6, 1993. The Office of the Assistant Secretary of Defense (Force Management and Personnel) responded that it had no comments to our draft report. See Part VI for the complete text of management comments.

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This report was prepared by the Financial Management Directorate, Office of the Assistant Inspector General for Auditing, DoD. Copies of the report can be obtained from the Secondary Reports Distribution Unit, Audit Planning and Technical Support Directorate, (703) 614-6303 (DSN 224-6303).

**Part I - Independent Auditor's Opinion
on the Financial Statements**

Introduction

The DoD Military Retirement Trust Fund was established in 1984 by Public Law 98-94 to provide retirement benefits for military personnel and their survivors. In FY 1992, the Fund paid \$24.6 billion to 1.5 million retirees and 181,000 survivors. As of September 30, 1992, the Fund's assets were \$106.1 billion, and its unfunded liability was \$411.9 billion. The Fund received revenue from three sources during FY 1992: contributions from the Services (\$16.3 billion), payments from the U.S. Treasury for the unfunded liability (\$11.2 billion), and interest earned on U.S. Treasury securities (\$9.4 billion). As of May 1993, a Fund manager had not been named. The Assistant Secretary of Defense (Force Management and Personnel) had been recommended to the Deputy Secretary of Defense for designation as the Fund manager; however, no official appointment had been made.

Financial statement audits such as this one are required by the Chief Financial Officers Act of 1990 (the CFO Act). The Principal Statements of the DoD Military Retirement Trust Fund are the responsibility of the Assistant Secretary of Defense (Force Management and Personnel) and the Defense Finance and Accounting Service. Our responsibility is to express an opinion on these financial statements, based on our audit.

Scope

We have audited the Principal Statements and the Notes to the Principal Statements of the DoD Military Retirement Trust Fund as of and for the year ended September 30, 1992. The Principal Statements include the Statement of Financial Position, Statement of Operations, Statement of Cash Flows, and Statement of Budget and Actual Expenses.

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in those statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial presentation of the statements. We believe that our audit provides a reasonable basis for our opinion. This financial statement audit was made between September 1992 and March 1993. See Part IV, Appendix B, for a list of organizations visited or contacted.

For this audit, we did not use an independent actuary to review and assess the actuarial methods, policies, and procedures used by the Office of the Actuary, DoD (the DoD Actuary). In FY 1991, the Chief Actuary of the Department of Labor (DoL) (the DoL Actuary) assisted the Office of the Assistant Inspector General for Auditing, DoD, by reviewing the actuarial methods, policies, and procedures used by the DoD Actuary to determine whether they complied with generally accepted actuarial principles. The DoL Actuary determined that the pension plan was administered in accordance with generally accepted actuarial principles, and that the actuarial present value of accumulated plan benefits was reasonable.

Independent Auditor's Opinion on the Financial Statements

For FY 1992, the economic assumptions used to calculate the "present value of accumulated plan benefits" changed from FY 1991. However, the DoD Actuary's computer program for calculating future plan benefits did not change. We limited our testing to any changes implemented by the DoD Actuary during FY 1992 that would have a direct and material impact on the financial statements. On April 9, 1993, the DoD Actuary notified the Office of the Assistant Inspector General for Auditing, DoD, that the DoD Board of Actuaries recommended changes to the interest rate and across-the-board salary scale assumptions that were used to calculate the "present value of accumulated plan benefits." The changes in these assumptions resulted in a decrease of \$28.9 billion to the actuarial "present value of plan benefits" on September 30, 1991. (In 1992, the DoD Actuary recalculated the amounts on the FY 1991 financial statements to account for the changed interest rates. The changes were made after we issued our FY 1991 audit report.) From our limited testing, we determined that the methods, policies, and principles had not changed from the preceding year, and we believe the financial information is accurate. However, our review of the actuarial methods, policies, and principles used by the DoD Actuary would not necessarily disclose all reportable conditions or weaknesses.

Auditing Standards

We conducted our audit in accordance with generally accepted Government auditing standards issued by the Comptroller General of the United States, as implemented by the IG, DoD, and Office of Management and Budget (OMB) Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Accounting Principles

Accounting principles are being studied by the Federal Accounting Standards Advisory Board. Generally accepted accounting principles for Federal entities will be promulgated by the Joint Financial Management Improvement Program principals, based on advice from the Board. In the interim, Federal agencies are to use a comprehensive basis of accounting as defined in OMB Bulletin No. 93-02, "Form and Content of Agency Financial Statements," October 22, 1992. The summary of significant policies, included in the Notes to the Principal Statements, describes the principles and methods of applying those principles that management has concluded are the most appropriate for presenting the Fund's significant assets, liabilities, net position, results of operations, cash flows, and reconciliation to budget.

Unqualified Opinion

In our opinion, the Principal Statements, including the Notes to the Principal Statements, present fairly, in all material respects, the assets, liabilities, and net financial position of the DoD Military Retirement Trust Fund as of September 30, 1992, and the results of operations, cash flows, and statement of budget and actual expenses for the year ended September 30, 1992, in accordance with DoD accounting policies and procedures and generally accepted accounting principles.

Additional Information

Our audit was conducted for the purpose of forming an opinion on the Principal Statements described above. We have reviewed the financial information presented in management's Overview of the Fund. The information in the Overview is presented for the purpose of additional analysis. We have not audited this information; therefore, we are not expressing an opinion on it. This information is addressed, however, in Part III, Compliance with Laws and Regulations, in accordance with OMB Bulletin No. 93-06, Section 6.a.(4) and (5).

Part II - Internal Controls

Introduction

We have audited the Principal Statements and the Notes to the Principal Statements contained in the DoD Military Retirement Trust Fund (the Fund) as of and for the year ended September 30, 1992.

Fund managers are responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, management is required to make estimates and judgments to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable but not absolute assurance that obligations and costs comply with applicable laws; that funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and that revenues and expenditures applicable to Fund operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports to maintain accountability over assets.

Objectives and Scope

Our audit objective was to determine whether there were adequate controls over the Fund to ensure that the financial statements were free of material error. In planning and performing our audit of the Principal Statements of the Fund for the year ended September 30, 1992, we considered its internal control structure. Our purposes were to determine the auditing procedures we would use to express our opinion on the Principal Statements, and to determine whether the internal control structure provided reasonable assurance that the financial statements were free of material misstatement. We obtained an understanding of the internal control policies and procedures; assessed the level of control risk for all significant cycles, classes of transactions, or account balances; and for those significant internal control policies and procedures that have been properly designed and placed in operation, we performed sufficient tests to provide reasonable assurance that the controls were effective and working as designed.

We classified the significant internal controls, policies, and procedures into the following four categories:

- Investments: policies, procedures, and internal controls over the receipt, investment, and transfer of funds by the Defense Accounting Office, Arlington.
- Contributions: policies, procedures, and internal controls over the Services' contributions to the Fund.
- Payments: policies, procedures, and internal controls over the disbursement of funds to retirees and annuitants, accounts receivable due the Fund, and Service contributions transferred to the Fund by Defense Finance and Accounting Service Centers.

- Actuarial: policies, procedures, and internal controls over the preparation of the actuarial projections by the DoD Actuary, including the present value of accumulated plan benefits and any changes in the present value of accumulated plan benefits.

We conducted our audit in accordance with generally accepted Government auditing standards issued by the Comptroller General of the United States, as implemented by the IG, DoD, and Office of Management and Budget (OMB) Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Principal Statements are free of material misstatement.

Prior Audit Coverage

The General Accounting Office and the IG, DoD, have issued two reports on the Military Retirement System. General Accounting Office (GAO) Report No. AFMD-87-35, "Military Retirement System's Financial Statements for Fiscal Year 1985," August 8, 1987, reported that interest was not charged on accounts receivable for overpayments of benefits. In our audit of the FY 1991 DoD Military Retirement Trust Fund Financial Statements, we found that an overall Fund manager had not been designated; that the DoD Actuary and the Defense Manpower Data Center (DMDC) had not implemented an internal control program; and that no internal controls existed over verification of Service contributions to the Fund.

We found that interest was not charged on all retirees' debts. See Part III, "Compliance with Laws and Regulations," for further details. Also, as of May 1993, a Fund manager had not been named. The Assistant Secretary of Defense (Force Management and Personnel) had been recommended to the Deputy Secretary of Defense for designation as the Fund manager; however, no official appointment had been made. Our FY 1992 audit found that the DoD Actuary and the DMDC had implemented an internal control program. The Director, Defense Finance and Accounting Service, had also implemented internal controls to verify contributions to the Fund.

Results of Audit

Our review of internal controls for the Fund did not disclose any material internal control weaknesses as defined in Public Law 97-255, "Federal Managers' Financial Integrity Act," Office of Management and Budget (OMB) Circular No. A-123, and DoD Directive 5010.38, "Internal Management Control Program," April 14, 1987. We also did not identify any conditions that we considered to be reportable under OMB Bulletin No. 93-06. Reportable conditions are significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the organization's ability to ensure that obligations and costs were in compliance with applicable

Internal Controls

laws; that funds, property, and other assets were safeguarded against waste, loss, unauthorized use, or misappropriation; and that revenues and expenditures applicable to agency operations were properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports in accordance with applicable accounting standards and to maintain accountability over assets.

A material weakness is a reportable condition in which the design or operation of the internal control structure does not reduce to a relatively low level the risk that errors or irregularities could occur. Such errors or irregularities would be in amounts material in relation to the statements being audited, or material to a performance measure or an aggregation of related performance measures, and might not be detected in a timely manner by employees in the normal course of performing their assigned functions.

At DFAS Centers, we found duplicate payments to three retirees. These lapses in controls were not material to the Fund; however, they require disclosure.

As part of our audit plan to test for fraud, waste, and abuse, we reviewed the data base of retirees who receive pension payments by mail. We tested for multiple payments to one address and to the same individual. In the Army, the Navy, and the Marine Corps, we found that one retiree in each Service was receiving duplicate payments. The Army retiree received duplicate payments for about 3 years, resulting in a total overpayment of \$29,691.44. The Marine Corps retiree received duplicate payments for about 12 years, and the total overpayment was \$60,655.26. The Navy retiree had recently retired, and had received one duplicate check which he returned during the period of our audit; therefore, no overpayment occurred.

In all three cases, the data base contained an erroneous Social Security number (SSN) in the retiree's name. Because only one or two digits in the SSNs were incorrect, processing clerks did not recognize the error. Internal controls over the payment system identified the potential duplicate records; however, because each SSN was similar to the retiree's actual SSN, the clerks believed the internal control reports were in error and established duplicate accounts. The Army and Marine Corps overpayments had been stopped as a result of our finding, and collection action had begun. The Army and Marine Corps cases had also been referred for criminal investigation.

We also noted internal control weaknesses over debt collection techniques, as discussed in Part III of this report, that were not material to the financial statements.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions, and would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. Part III,

Compliance with Laws and Regulations, addresses noncompliance with the Debt Collection Act of 1982. This noncompliance is also an internal control weakness. Except for the matters noted in Part III, we believe there is reasonable assurance that the internal control structure meets the control objectives.

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Part III - Compliance with Laws and Regulations

Introduction

We have audited the Principal Statements and the Notes to the Principal Statements for the DoD Military Retirement Trust Fund as of and for the year ended September 30, 1992. Financial statement audits such as this one are required by the Chief Financial Officers Act of 1990.

Objectives and Scope

Our objective was to assess compliance with laws and regulations for transactions and events that have a direct and material effect on the financial statements. Material instances of noncompliance are failures to follow requirements, or violations of prohibitions contained in laws or regulations, that cause us to conclude that the aggregation of the material misstatements resulting from those failures or violations is material to the Principal Statements, or that the sensitivity of the matter would cause it to be perceived as significant by others and may affect the financial statement opinion.

The Assistant Secretary of Defense (Force Management and Personnel) and the Director, Defense Finance and Accounting Service (DFAS), are responsible for compliance with laws and regulations applicable to the Fund. To obtain reasonable assurance about whether the Principal Statements were free of material misstatement, we tested compliance with laws and regulations that may directly affect the financial statements, and with certain other laws and regulations designated by the Office of Management and Budget and DoD (see Part IV, Appendix A). We reviewed management's procedures for evaluating and reporting on internal controls and accounting systems as required by the Federal Managers' Financial Integrity Act (FMFIA), and we compared the Fund's most recent FMFIA reports with our evaluation of the internal control system. We also reviewed and tested the Fund's policies, procedures, and systems for documenting and supporting financial, statistical, and other information presented in the Overview of financial statements. However, our objective was not to provide an opinion on overall compliance with such laws and regulations.

The audit was made in accordance with generally accepted Government auditing standards issued by the Comptroller General of the United States, as implemented by the IG, DoD, and Office of Management and Budget (OMB) Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Principal Statements are free of material misstatement.

Prior Audit Coverage

Between 1987 and 1993, the General Accounting Office (GAO); the Service audit organizations; and the IG, DoD, issued four audit reports addressing DFAS's failure to assess interest, penalties, and administrative charges on retirees' debts. The audit agencies recommended that interest be charged on retired pay debts, that debtors be charged administrative fees, and that penalties be assessed on delinquent debts. The IG, DoD recommended that the Director, DFAS, centralize management over DoD's debt collection functions and develop uniform operating procedures. GAO Report No. AFMD-87-35, "Military Retirement System's Financial Statements for Fiscal Year 1985," August 8, 1987, reported that interest was not charged on accounts receivable for overpayment of benefits. Air Force Audit Agency Report No. 100-0-14, "Interest Assessed on Debts Owed the Air Force, Air Force Accounting and Finance Center," January 22, 1990, stated that the Air Force did not assess interest on debts when necessary. We found similar conditions during our audit. See Results of Audit for further details.

Results of Audit

Our tests of compliance with laws and regulations did not disclose any material weaknesses affecting the financial statements. However, three instances of noncompliance came to our attention. P.L. 98-94, the "Department of Defense Authorization Act of 1983," which required rounding down of retiree entitlements, was not implemented in a timely manner. P.L. 97-365, the "Debt Collection Act of 1982," was not consistently applied to retiree debts at the DFAS Centers. We also found that the statements failed to disclose certain information required by OMB Bulletin No. 93-02, "Form and Content of Agency Financial Statements," October 22, 1992.

Implementing the Defense Authorization Act. During this audit, we conducted a separate review of the effectiveness of the implementation of P.L. 98-94 at DFAS-Denver. P.L. 98-94 required retirees' pay entitlements to be rounded down to whole dollar amounts. The Retired Pay Systems Development Support Division failed to update the Retired Pay System when P.L. 98-94 was passed in September 1983, but corrected the condition in November 1992. The noncompliance existed in FY 1992 and caused retirees to be overpaid about \$16 million during a 9-year period. To correct the noncompliance, the Retired Pay Division updated its accounting system in November 1992 and sent letters to retirees explaining the overpayments. See Report No. 93-085, "Results of Review of the Implementation of P.L. 98-94 for Air Force Retirees," for further details.

Implementing the Debt Collection Act of 1982. The Retired Pay Divisions at the DFAS Centers had not fully complied with laws and regulations on debt collection. The DFAS Centers had not implemented controls to ensure that interest, penalties, and administrative charges were consistently assessed on

debts owed by retirees. Further, procedures such as write-offs were not used aggressively, and were not reported to the Internal Revenue Service (IRS) on IRS Form 1099-G, "Certain Government Payments." As a result, retirees were receiving interest-free loans at taxpayer expense, and the IRS could not assess taxes because the debts had not been written off.

Background. Collecting debts from the public sector has been a continuing problem for Federal agencies. P. L. 97-365 authorizes Federal agencies to assess interest, penalties, and administrative charges on debts owed by individuals. Debt collection managers can charge penalties on debts more than 90 days delinquent, and administrative charges can be assessed to cover the costs of processing debts. Assessing penalties and administrative charges encourages individuals to pay their debts promptly.

DoD Directive 7045.13, "DoD Credit Management and Debt Collection Program," October 31, 1986, establishes debt collection policies and procedures for DoD and assigns responsibility for debt collection within DoD. DoD Instruction 7045.18, "Collection of Indebtedness Due the United States," March 13, 1985, establishes responsibilities for the collection of debts owed by DoD personnel. OMB Circular No. A-129, "Managing Federal Credit Programs," November 25, 1988, explains procedures for collecting debts, such as the assessment of interest, penalties, and administrative fees. OMB Circular No. A-129 also establishes procedures for write-offs and the use of IRS Form 1099-G for collection action by the IRS. This guidance requires DoD agencies to pursue debts promptly.

Discussion of Details. We tested the retirees' debts to determine whether the DFAS Centers were assessing interest, penalties, and administrative charges. Retirees incur debts when they receive overpayments of active duty benefits or retirement pay, or when they exceed the limitations imposed by 5 U.S.C. 5532, "Employment of Retired Members of the Uniformed Services." Under 5 U.S.C. 5532 retirees may be subject to reductions in their retired pay when they are employed by the Federal Government. We found that interest was not charged consistently on retirees' debts. For example, DFAS-Indianapolis assessed interest on most categories of retirees' debts, but did not assess it consistently in all cases. DFAS-Cleveland assessed interest on some annuities and benefit plans. DFAS-Kansas City assessed interest only on some benefit plans. DFAS-Denver assessed interest on some benefit plans, Dual Compensation debts, and Pay Cap debts over 1 year old. Where applicable, penalties and administrative charges were not assessed on debts as required by the Debt Collection Act of 1982. Except for DFAS-Kansas City, accounting systems at the DFAS Centers could automatically assess interest, penalties, and administrative charges on debts.

With the exception of DFAS-Kansas City, the DFAS Centers did not report uncollectible or written-off retiree debts to the IRS as taxable income, as required by OMB Circular No. A-129. Income taxes should be assessed on amounts that are uncollectible or written off by the DFAS Centers. A test of write-offs from DFAS-Indianapolis showed that some debts were 10 years old, and that IRS Forms 1099-G had not been sent to the IRS. When asked about

the IRS Forms 1099-G, managers at DFAS-Indianapolis said that the overpayments had already been reported on IRS Forms W-2P or 1099-R (forms that are issued to retirees to show the amount of retirement income reported to the IRS), and that issuing IRS Forms 1099-G the following year would subject retirees to double taxation. The statement that retirees would be subject to double taxation is correct; however, failure to send the IRS Forms 1099-G to the IRS is inconsistent with proper debt collection practices. The retirees were not entitled to the overpayments; therefore, the overpayments should not have been reported on IRS Forms W-2P or 1099-R. DFAS-Indianapolis should have issued amended IRS Forms W-2P or 1099-R to employees, subtracting the overpayments, and should have taken collection action. Because DFAS-Indianapolis did not try to collect the overpayments directly, the Government may have received only a small portion of the debts owed by retirees, and the Fund may not have recovered payments made erroneously.

Although this failure to collect debts owed by retirees does not materially affect the Fund's financial statements, the lack of action violates the public law, deprives the Government of funds, and should be corrected. This problem was discussed in our Audit Report No. 92-021, "Debt Collection and Deposit Controls," December 13, 1991.

Compliance with OMB Bulletin No. 93-02. The statements do not properly report on certain information that was required by OMB Bulletin No. 93-02. Although the noncompliances were not material to the opinion, OMB Bulletin No. 93-02 requires that certain information be included in order to improve the usefulness of the statements. The list of deficiencies is shown below.

- o The statements do not show the cost of administering the military retirement system. Our audit showed that in FY 1992 the Centers incurred costs of about \$45.2 million to administer retirees' and annuitants' benefits.

- o The statements include a performance measure on the ratio of assets in the Fund to the present value of future benefits for annuitants covered by the Fund. This performance measure provides useful information to the reader. OMB Bulletin No. 93-02 requires that the Overview include a discussion and analysis of the reporting entity's financial condition. We believe further financial information and analysis would improve the usefulness of the statements.

The results of our tests indicate that with respect to the items tested, except for noncompliances with P.L. 98-94, P.L. 97-365, and OMB Bulletin No. 93-02, the Fund complied in all material respects with the provisions referred to in the Objectives and Scope. With respect to items not tested, nothing came to our attention that caused us to believe that the DoD Components operating the Fund had not complied, in all material respects, with the provisions identified above.

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Part IV - Additional Information

Appendix A. Laws and Regulations

Uniformed Services Contingency Option Act of 1953, P.L. 83-239

Armed Forces-Retired Pay Act of 1961, P.L. 87-381

Uniform Services Pay Act of 1963, P.L. 88-132

Dual Compensation Act of 1964, P.L. 88-448

Survivor Benefit Plan Act of 1972, P.L. 92-425

Civil Service Reform Act of 1978, P.L. 95-454

Personnel Management Act of 1981, P.L. 96-513 ¹

Federal Managers' Financial Integrity Act of 1982, P.L. 97-255

Debt Collection Act of 1982, P.L. 97-365

Department of Defense Authorization Act of 1983, P.L. 98-94 ²

Omnibus Budget Reconciliation Act of 1983, P.L. 98-270 ³

Deficit Reduction Act of 1984, P.L. 98-369 ⁴

Public Debt Limit - Balanced Budget & Emergency Deficit Control Act of 1985,
P.L. 99-177

Chief Financial Officers Act of 1990, P.L. 101-576

Title 2 of the General Accounting Office's "Policies and Procedures Manual for
Guidance of Federal Agencies," August 1987

OMB Circular A-123, "Internal Control Systems," August 4, 1986

OMB Bulletin No. 93-02, "Form and Content of Agency Financial Statements,"
October 22, 1992

OMB Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements,"
January 8, 1993

DoD Manual 7220.9-M, "DoD Accounting Manual," October 1983

DoD Directive 5010.38, "Internal Management Control Program," April 14, 1987

¹ Changed computation method to high 36 months' pay.

² Established the DoD Military Retirement Trust Fund.

³ Current provision for year-end cost-of-living allowance.

⁴ Made entitlements payable at the beginning of each month.

Appendix B. Organizations Visited or Contacted

Office of the Secretary of Defense

Office of the Assistant Secretary of Defense (Force Management and Personnel),
Washington, DC
Defense Manpower Data Center, Arlington, VA
Defense Manpower Data Center, Monterey, CA
Department of Defense, Office of the Actuary, Arlington, VA
Office of the Comptroller of the Department of Defense, Washington, DC

Department of the Army

National Guard Bureau, Army Comptroller Directorate, Washington, DC
Office of the Chief of Army Reserve, Comptroller Division, Washington, DC
Army Reserve Personnel Center, St. Louis, MO
Army National Guard Personnel Center, Alexandria, VA

Department of the Navy

Bureau of Naval Personnel, Arlington, VA
Naval Reserve Personnel Center, New Orleans, LA
Deputy Chief of Staff for Finance, Naval Reserve Force, Budget Division, New Orleans, LA
Manpower and Reserve Affairs, Personnel Management Division, Quantico, VA

Department of the Air Force

Air Force Military Personnel Center, San Antonio, TX
Air Force Reserve Personnel Center, Denver, CO

Marine Corps

Headquarters, Marine Corps, Arlington, VA

Appendix B. Organizations Visited or Contacted

Other Defense Organizations

Headquarters, Defense Finance and Accounting Service, Washington, DC
Defense Finance and Accounting Service - Cleveland Center, Cleveland, OH
Defense Accounting Office, Arlington, VA
Defense Finance and Accounting Service - Denver Center, Denver, CO
Defense Finance and Accounting Service - Indianapolis Center, Indianapolis, IN
Defense Finance and Accounting Service - Kansas City Center, Kansas City, MO

Non-Defense Federal Organizations

National Personnel Records Center, St. Louis, MO

Appendix C. Report Distribution

Office of the Secretary of Defense

Secretary of Defense
Deputy Secretary of Defense
Assistant Secretary of Defense (Force Management and Personnel)
Assistant Secretary of Defense (Public Affairs)
Assistant Secretary of Defense (Reserve Affairs)
Comptroller and Chief Financial Officer of the Department of Defense

Department of the Army

Auditor General, U.S. Army Audit Agency
Inspector General of the Army
Office of the Chief of Army Reserve, Comptroller Division
Chief, Army Comptroller Directorate, National Guard Bureau

Department of the Navy

Assistant Secretary of the Navy (Financial Management)
Comptroller of the Navy
Auditor General, Naval Audit Service
Deputy Chief of Staff for Finance, Naval Reserve Force

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and Comptroller)
Auditor General, U.S. Air Force Audit Agency

Other Defense Organizations

Director, Defense Finance and Accounting Service
Director, Defense Finance and Accounting Service - Cleveland Center
Director, Defense Finance and Accounting Service - Denver Center
Director, Defense Finance and Accounting Service - Indianapolis Center
Director, Defense Finance and Accounting Service - Kansas City Center

Appendix C. Report Distribution

Non-Defense Federal Organizations

Office of Management and Budget
U.S. General Accounting Office
NSIAD Technical Information Center

Chairmen and Ranking Minority Members of each of the following Congressional Committees and Subcommittees:

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Subcommittee on Manpower and Personnel, Committee on Armed Services
Senate Committee on Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Subcommittee on Military Personnel and Compensation, Committee on Armed Services
House Committee on Government Operations
House Subcommittee on Legislation and National Security, Committee on Government Operations

**Part V - DoD Military Retirement Trust
Fund Financial Statements for
FY 1992**

DoD Military Retirement Trust Fund Financial Statements for FY 1992



OFFICE OF THE COMPTROLLER OF THE DEPARTMENT OF DEFENSE

WASHINGTON, DC 20301-1100

JUN 17 1993


MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING, DOD

SUBJECT: Transmittal of the DoD Military Retirement Trust Fund
Financial Statements on FY 1992 Financial Activity

On March 23, 1993, the DoD Military Retirement Trust Fund financial statements on FY 1992 financial activity were submitted for audit as required by the Chief Financial Officers Act of 1990. The financial statements were incomplete as discussed in DoDIG memorandum dated, May 6, 1990. The following changes have been made and are included in the attached final report:

- The Principal Statements show comparative data from FY 1991.
- Footnote 1 has been expanded to clarify that the financial statements are presented on the accrual basis of accounting.
- Corrections to "Interest Income" have been accomplished as requested in the DoDIG memorandum.

My point of contact on this matter is Mr. Oscar Covell. He may be reached on 697-6149.


Alvin Tucker
Acting Chief Financial Officer

Attachment

DoD Military Retirement Trust Fund Financial Statements for FY 1992

DOD Military Retirement Trust Fund

Table of Contents

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***DOD MILITARY
RETIREMENT TRUST
FUND***

OVERVIEW

DoD Military Retirement Trust Fund Financial Statements for FY 1992

Overview 3

SUMMARY OF THE MILITARY RETIREMENT SYSTEM

As of September 30, 1992

OVERVIEW

The military retirement system applies to the Army, Navy, Marine Corps, and Air Force. However, most of the provisions also apply to retirement systems for members of the Coast Guard (administered by the Department of Transportation), officers of the Public Health Service (administered by the Department of Health and Human Services), and officers of the National Oceanic and Atmospheric Administration (administered by the Department of Commerce). Those not in plans administered by the Department of Defense are not included in this valuation.

The system is a funded, noncontributory, defined-benefit plan that includes nondisability retired pay, disability retired pay, retired pay for reserve service, and survivor annuity programs. The Service Secretaries approve immediate nondisability retired pay at any age with credit of at least 20 years of active-duty service. Reserve retirees must be 60 years old with 20 creditable years of service before retired pay commences. There is no vesting before retirement.

There are three distinct nondisability benefit formulas (relevant to three distinct populations) within the military retirement system. Military personnel who first became members of the Armed Services before September 8, 1980 have retired pay equal to (terminal basic pay) times (a multiplier). The multiplier is equal to (2.5%) times (years of service) and is limited to 75%. If the retiree first became a member of the Armed Services on or after September 8, 1980, the average of the highest 36 months of basic pay is used instead of terminal basic pay. Members first entering the Armed Services on or after August 1, 1986 are subject to a penalty if they retire with less than 30 years of service; at age 62, their retired pay is recomputed without the penalty.

Retiree and survivor benefits are automatically adjusted annually to protect the purchasing power of initial retired pay. The benefits associated with members first entering the Armed Services before August 1, 1986 are adjusted by the percentage increase in the average Consumer Price Index (CPI). This is commonly referred to as full CPI protection. Benefits associated with members entering on or after August 1, 1986 are annually increased by the percentage change in the CPI minus 1%. At the military member's age 62, the benefits are restored to the amount that would have been payable had full CPI protection been in effect. This restoral is in combination with that described in the previous paragraph. However, after this restoral, partial indexing (CPI minus 1%) continues annually for life.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

4 Overview

Nondisability Retirement From Active Service

The current system allows voluntary retirement upon completion of at least 20 years of service at any age, subject to Service Secretary approval. The military retiree receives immediate retired pay calculated as (base pay) times (a multiplier). Base pay is equal to terminal basic pay if the retiree first became a member of the Armed Services before September 8, 1980. It is equal to the average of the highest 36 months of basic pay for all other members. The multiplier is equal to (2.5%) times (years of service, rounded down to the nearest month) and is limited to 75%. Members first entering the Armed Services on or after August 1, 1986, and who retire with less than 30 years of service receive a temporary penalty until age 62. The penalty reduces the multiplier by one percentage point for each full year under 30. For example, the multiplier for a 20-year retiree would be 40% (50% minus 10%). At age 62, the penalty is removed and the retired pay is restored.

In FY 92, 1.20 million nondisability retirees from active duty were paid \$20.17 billion.

Disability Retirement

A disabled military member is entitled to disability retired pay if the disability is at least 30% (under a standard schedule of rating disabilities by the Veterans Administration) and either (1) the member has eight years of service; (2) the disability results from active duty; or (3) the disability occurred in the line of duty during a time of war or national emergency or certain other time periods.

In disability retirement, the member receives retired pay equal to the larger of (1) the accrued nondisability retirement benefit, or (2) base pay multiplied by the rated percent of disability. The benefit cannot be more than 75% of base pay. Only the excess of (1) over (2) is subject to Federal income taxes. Base pay is equal to terminal basic pay if the retiree first became a member of the Armed Services before September 8, 1980. If the retiree first entered the Services on or after September 8, 1980, base pay is equal to the average of the highest 36 months of basic pay.

Members whose disability may not be permanent are placed on a temporary-disability retired list and receive disability retirement pay just as if they were permanently disabled. However, they must be physically examined every 18 months for any change in disability. A final determination must be made within five years. The temporary-disability pay is calculated like the permanent-disability retired pay, except that it can be no less than 50% of base pay.

In FY 92, 130,000 disability retirees were paid \$1.52 billion.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

Overview 5

Reserve Retirement

Members of the reserves may retire after 20 years of creditable service, the last eight of which must be in a reserve component. However, reserve retired pay is not payable until age 60. Retired pay is computed as (base pay) times (2.5%) times (years of service). If the reservist was first a member of the Armed Services before September 8, 1980, base pay is defined as the active duty basic pay in effect for the retiree's grade and years of service at the time that retired pay begins. If the reservist first became a member of the Armed Services on or after September 8, 1980, base pay is the average basic pay for the member's grade in the last three years that he/she was a member of the Armed Services. In effect, the retired pay of any member who entered the Armed Forces on or after September 8, 1980, and who later separates from a reserve component before turning 60 is based on active duty pay at the time of separation.

The years of service are determined by using a point system, where 360 points convert to a year of service. Typically, a point is awarded for a day of service or a drill attendance, with 15 points being awarded for a year's membership in a reserve component. A creditable year of service is one in which the member earned at least 50 points. A member cannot retire without 20 creditable years, although points earned in non-creditable years are used in the retirement calculation.

In FY 92, 193,000 reserve retirees were paid \$1.76 billion.

Survivor Benefits

Legislation originating in 1953 provided optional survivor benefits. It was later referred to as the Retired Servicemen's Family Protection Plan (RSFPP). The plan proved to be expensive and inadequate since the survivor annuities were never adjusted for inflation and could not be more than 50% of retired pay. RSFPP was designed to be self-supporting in the sense that the present value of the reductions to retired pay equalled the present value of the survivor annuities. However, no fund was involved.

Since September 21, 1972, RSFPP has been replaced by the Survivor Benefit Plan (SBP) for new retirees. RSFPP still covers those servicemen retired before 1972 who did not convert to the new plan and still pays survivor annuities.

Retired pay is reduced, before taxes, for the member's cost of SBP. Total SBP costs are shared by the Government and the retiree, so the reductions in retired pay are only a portion of the total cost of the SBP program.

The SBP survivor annuity is initially 55% of the member's base amount. The base amount is elected by the member, but cannot be less than \$300 or more than the member's full retired pay. If a penalty for service under 30 years is included in the calculation of retired pay, the maximum base amount is equal to the full retired pay without the penalty.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

6 Overview

The spouse's annuity is considered a two-tier benefit because, at age 62, the annuity is reduced to 35% of the base amount. Prior to the enactment of the two-tier benefit, the survivor annuity was integrated with Social Security. SBP participants and active and reserve personnel with at least 20 years of service on October 1, 1985 were grandfathered into the two-tier system. Their survivors will be given the higher of the two annuities.

During FY 87 a change was made to the SBP that increased benefits for survivors. Prior to FY 87, a widow remarrying before age 60 lost her survivor annuity. The age after which there is no loss of benefits to a surviving spouse who remarries has been reduced from age 60 to 55.

In FY 90 SBP premiums were lowered to 6.5 percent of the member's base amount and a supplementary benefit was introduced to allow members to increase their survivors' second-tier 35% benefit to 55%. The cost of the supplementary benefit is to be borne entirely by members in the form of actuarial, age-specific premiums. Because of these changes, an open season is scheduled from April 1, 1992, through March 31, 1993, to afford retirees with SBP the opportunity to increase their current coverage and retirees without SBP to elect in.

Members who die on active duty with over 20 years of service are assumed to have retired on the day they died and to have elected full SBP coverage for spouses and/or children.

SBP annuities are reduced by veteran's survivor benefits and all premiums relating to the reductions are returned to the widow. Additionally, SBP annuities are annually increased with cost-of-living adjustments (COLAs). These COLAs may be based on full or partial Consumer-Price-Index increases, depending on when the member first entered the Armed Services. If the member dies before age 62 and the survivor is subject to partial COLAs, the survivor's annuity is increased (on the member's 62nd birthday) to the amount that would have been payable had full COLAs been in effect. Partial COLAs continue annually thereafter.

For reserve retirees, the same set of retired pay reductions apply to survivor coverage after the reservist reaches age 60 (when the reservist begins to receive retired pay). A second set of optional reductions (funded by the member only) extends this coverage to reservists who have enough service to retire, but have not attained age 60. The added cost of the pre-age 60 coverage is deducted from the member's retired pay and the survivor's annuity.

In FY 92, 181,000 surviving families were paid \$1.13 billion.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

Overview 7

Cost-of-Living Increases

All nondisability retirement, disability retirement, and most survivor annuities are adjusted annually for inflation. Cost-of-living adjustments (COLA) are automatically scheduled to occur every 12 months, on December 1st, to be reflected in checks issued at the beginning of January.

The "full" COLA increase effective December 1st is computed by calculating the percentage increase in the Consumer Price Index from the third quarter of the prior calendar year to the third quarter of the current calendar year. The increase is based on the Urban Wage Earner and Clerical Worker Consumer Price Index (CPI-W) and is rounded to the nearest 1/10 of one percent.

The benefits of retirees (and their survivors) first entering the Armed Services before August 1, 1986 are annually increased with the full COLA; all other benefits are annually increased with a "partial" COLA. The partial COLA is the full COLA minus 1%. A onetime restoral is given to a partial-COLA recipient on the first day of the month after the retiree's 62nd birthday. At this time, the retiree benefit (or survivor benefit if the retiree is deceased) is increased to the amount that would have been payable had full COLAs been in effect. Annual partial COLAs continue after this restoral.

Relationship with Veterans Administration Benefits

The Veterans Administration (VA) provides compensation for Service-connected and certain non-Service-connected disabilities. These VA benefits can be in place of (or in combination with) DoD retired pay, but they are not additive. Since VA benefits are exempt from Federal income taxes, it is sometimes to the advantage of a member to elect them.

Veterans Administration benefits also overlap survivor benefits through the Dependence and Indemnity Compensation (DIC) program. DIC is payable to survivors of veterans who died from Service-connected causes. A reduction of this amount is made to the SBP annuity; however, all premiums relating to the reductions are returned to the widow.

Interrelationship with Other Federal Service

For retirement purposes, no credit is given for other Federal service, except where cross-service transferability is allowed. Military service is generally creditable toward the Federal civilian retirement systems if military retired pay is waived. However, a deposit (equal to a percentage of post-1956 basic pay) must be made to the Civil Service Retirement Fund in order to receive credit. Military service is not generally creditable under both systems (but is for reservists and certain disability retirees). Retired regular officers employed by the Federal Government lose a substantial portion of their retired pay while

DoD Military Retirement Trust Fund Financial Statements for FY 1992

8 Overview

so employed, and most retired members are subject to a combined ceiling equivalent to Level V of the Executive Schedule. The ceiling does not apply to those who had retired before October 13, 1978 (or were under age 60 and eligible for Reserve retirement on that date) and were continuously employed by the Federal Government since that date.

Relationship of Retired Pay to Military Compensation

Basic pay is the only element of military compensation upon which retired pay is computed and entitlement is determined. Basic pay is the principal element of military compensation that all members receive; but it is not representative, for comparative purposes, of salary levels in the public or private sectors. Reasonable comparisons can be made, however, to basic military compensation (BMC) or regular military compensation (RMC). BMC is the sum of basic pay, the quarters allowance (either cash or in kind), a subsistence allowance (either cash or in kind), and the Federal tax advantages accruing to allowances, since they are not subject to Federal income tax. RMC is BMC plus the average variable housing allowance (which varies by location) and the additional tax advantage it brings. Basic pay represents approximately 77% of BMC or 73% of RMC for all retirement eligibles. For the 20-year retiree, basic pay is approximately 75% of BMC or 71% of RMC. Consequently, a 20-year retiree may be entitled to 50% of basic pay, but only 37% of BMC or 35% of RMC. For a 30-year retiree the corresponding entitlements are 75% of basic pay but only 60% of BMC or 57% of RMC. These relationships should be considered when military retired pay is compared to compensation under other retirement systems.

Changes in Actuarial Assumptions for the Plan Year Ended September 30, 1991

For the actuarial valuation as of September 30, 1991, the DoD Board of Actuaries made significant changes in the actuarial assumptions. In regard to the economic assumptions, the interest rate was changed from 7% to 7.5%, and the across-the-board salary increases were changed from 5.75% to 5.5%. These changes combined to reduce the present value of accumulated plan benefits. In addition, changes were made to many of the non-economic or decrement assumptions. The effect of these changes was to increase the present value of accumulated plan benefits, but their effect was outweighed by the changes to the economic assumptions.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

Overview 9

Performance Measures

While there are many ways to measure the funding progress of a pension plan, the ratio of assets in fund to the value of future benefits for annuitants on the roll is commonly used. Here is how this ratio has looked for the past seven years:

- a. September 30, 1992 = .27018
- b. September 30, 1991 = .25127
- c. September 30, 1990 = .21878
- d. September 30, 1989 = .19549
- e. September 30, 1988 = .16211
- f. September 30, 1987 = .11431
- g. September 30, 1986 = .07187

The 27% ratio as of September 30, 1992 is still low as far as most pension plans go, but the above numbers display the continuing improvement in the measure after a late start in funding.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

10 Overview

DEPARTMENT OF DEFENSE MILITARY RETIREMENT FUND STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS (\$ in thousands)

| | For the Plan Year Ended: | |
|---|--------------------------|---------------|
| | Sept 30, 1992 | Sept 30, 1991 |
| Assets | | |
| Investments, at fair market value U.S. Government securities ¹ | \$122,147,022 | \$102,906,263 |
| Accounts receivable Accrued interest ² | 3,694,233 | 3,285,566 |
| Due from Military Retirees or their Survivors | 31,017 | 27,882 |
| Cash | 14,937 | 28 |
| Total Assets | \$125,887,208 | \$106,219,739 |
| Accounts Payable | 2,096,145 | 2,028,043 |
| Total Assets Available for Benefits | \$123,791,063 | \$104,191,696 |

¹Fair market value of securities has been measured by quoted prices (bid price) in the active U.S. Government securities market. Bid price used represents the over-the-counter quotations as of 4 PM Eastern time, as reported in the Wall Street Journal on October 1, 1992.

²Includes accrued interest receivable (including interest purchased).

DoD Military Retirement Trust Fund Financial Statements for FY 1992

Overview 11

DEPARTMENT OF DEFENSE MILITARY RETIREMENT FUND STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS (\$ in thousands)

| | For the Plan Year Ended: | |
|---|--------------------------|---------------|
| | Sept 30, 1992 | Sept 30, 1991 |
| Net assets avail. for benefits at beginning of plan year | \$104,191,696 | \$81,900,699 |
| Investment income | | |
| Interest | 10,018,052 | 8,951,217 |
| Net apprec. (deprec.) in fair market value of investment ¹ | 6,655,296 | 8,606,030 |
| Contributions | | |
| From services | 16,314,155 | 17,192,667 |
| Appropriation to amortize unfunded liability | 11,169,000 | 10,782,000 |
| Transfer from Office of Personnel Management | | 101 |
| Total additions | \$44,156,503 | \$45,532,015 |
| Benefits paid to participants ² | 24,557,065 | 23,241,018 |
| Net assets available for benefits at end of plan year | \$123,791,135 | \$104,191,696 |

¹ Investments bought, sold and held during the plan year ended September 30 appreciated (depreciated) in value as follows:

| | PY 1992 | PY 1991 |
|--|--------------------|----------------------|
| Appreciated (depreciated) fair value over book value | \$7,298,488 | \$9,065,439 |
| Amortized discount | 17,245 | 568 |
| Amortized premium | (660,437) | (459,952) |
| Gain (loss) on sale | | (25) |
| | <u>\$6,655,296</u> | <u>(\$8,606,030)</u> |

² The statement has been adjusted to show benefits paid to participants on an accrual basis.

| | PY 1992 | PY 1991 |
|---|---------------------|---------------------|
| Benefits paid on cash basis | \$24,488,963 | \$23,089,316 |
| Increase in liability for benefits due at end of year | 68,102 | 151,702 |
| Benefits paid on accrual basis | <u>\$24,557,065</u> | <u>\$23,241,018</u> |

DoD Military Retirement Trust Fund Financial Statements for FY 1992

12 Overview

DEPARTMENT OF DEFENSE MILITARY RETIREMENT FUND STATEMENT OF ACCUMULATED PLAN BENEFITS (\$ in billions)

| ACCUMULATED PLAN BENEFITS ¹ | For The Plan Year Ended: | |
|--|--------------------------|---------------|
| | Sept 30, 1992 | Sept 30, 1991 |
| Actuarial present value of vested benefits | | |
| Participants currently receiving payments ² | \$392.7 | \$392.7 |
| Other vested participants | \$59.2 | \$59.1 |
| Total vested | \$451.9 | \$432.0 |
| Actuarial present value of nonvested benefits | \$64.0 | \$64.9 |
| Total actuarial present value of accumulated plan benefits | \$515.9 | \$496.9 |
| TOTAL ASSETS ² | \$125.9 | \$106.2 |
| EXCESS OF ACCUMULATED BENEFITS OVER NET ASSETS | \$390.0 | \$390.7 |

¹See definition of accumulated plan benefits on preceding page.

²Total assets are reported in this table because the liability for benefit payments due is included in the actuarial present value of benefits for participants currently receiving payments.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

Overview 13

MILITARY RETIREMENT SYSTEM STATEMENT OF CHANGES IN PRESENT VALUE OF ACCUMULATED PLAN BENEFITS (\$ in billions)

For the Plan Year Ended:
Sept 30, 1992 Sept 30, 1991

| | | |
|---|----------------|----------------|
| 1. Actuarial present value of accumulated plan benefits at beginning of plan year | \$496.9 | \$497.2 |
| 2. Increase (decrease) during the year ¹ attributable to: | | |
| a. Benefits accumulated and actuarial gain (loss) | 19.0 | 28.6 |
| b. Plan amendment(s) | | |
| c. Changes in actuarial assumptions | | (28.9) |
| 3. Net increase | <u>\$19.0</u> | <u>(\$0.3)</u> |
| 4. Actuarial present value of plan benefits at end of year | <u>\$515.9</u> | <u>\$496.9</u> |

¹The assumed order of occurrence was: (1) plan amendments, (2) changes in actuarial assumptions, and (3) benefits accumulated and actuarial gain (loss).

***DOD MILITARY
RETIREMENT TRUST
FUND***

PRINCIPAL STATEMENTS

DoD Military Retirement Trust Fund Financial Statements for FY 1992

Principal Statements 17

Department/Agency: DOD Military Retirement Trust Fund
Reporting Entity: Principal Statements
Statement of Financial Position
as of September 30, 1992
(Dollars)

| ASSETS | 1992 | 1991 |
|---|--------------------------|-----------------------|
| 1. Financial Resources: | | |
| a. Fund Balances with Treasury (Note 2) | \$14,936,765 | 28,256 |
| b. Cash | | |
| c. Foreign Currency | | |
| d. Other Monetary Assets | | |
| e. Investments, Non-Federal | | |
| f. Accounts Receivable, Net - Non-Federal | 31,017,427 | 27,881,910 |
| g. Inventories Held for Sale, Net | | |
| h. Loans Receivable, Net - Non-Federal | | |
| i. Advances and Prepayments, Non-Federal | | |
| j. Property Held for Sale | | |
| k. Other, Non-Federal | | |
| l. Intragovernmental Items: | | |
| (1) Accounts Receivable, Federal | 3,694,232,661 | 3,285,565,830 |
| (2) Loans Receivable, Federal | | |
| (3) Investments, Federal (Note 3) | 102,364,277,220 | 90,422,006,797 |
| (4) Other, Federal | | |
| m. Total Financial Resources | <u>\$106,104,464,073</u> | <u>93,735,482,793</u> |
| 2. Non-Financial Resources: | | |
| a. Resources Transferable to Treasury | | |
| b. Inventories Not Held for Sale | | |
| c. Property, Plant and Equipment, Net | | |
| d. Other | | |
| e. Total Non-Financial Resources | | |
| 3. Total Assets | <u>\$106,104,464,073</u> | <u>93,735,482,793</u> |
| | | |
| LIABILITIES | | |
| 4. Funded Liabilities | | |
| a. Accounts Payable, Non-Federal | | |
| b. Accrued Interest Payable | | |
| c. Accrued Payroll and Benefits | | |
| d. Accrued Entitlement Benefits | 2,096,145,177 | 2,028,042,903 |
| e. Lease Liabilities | | |
| f. Debt | | |
| g. Guarantees Payable | | |
| h. Other Funded Liabilities, Non-Federal (Note 4) | 104,008,318,896 | 91,707,439,890 |

The accompanying notes are an integral part of these statements.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

18 Principal Statements

Department/Agency: DOD Military Retirement Trust Fund
 Reporting Entity: Principal Statements
 Statement of Financial Position
 as of September 30, 1992
 (Dollars)

| LIABILITIES Continued | 1992 | 1991 |
|--|----------------------------|----------------------------|
| i. Intragovernmental Liabilities | | |
| (1) Accounts Payable, Federal | | |
| (2) Debt | | |
| (3) Deferred Revenue | | |
| (4) Other Funded Liabilities, Federal | | |
| j. Total Funded Liabilities | <u>\$106,104,464,073</u> | <u>93,735,482,793</u> |
| 5. Unfunded Liabilities: | | |
| a. Accrued Leave | | |
| b. Lease Liabilities | | |
| c. Pensions and Other | | |
| Actuarial Liabilities (Note 5) | 411,891,681,104 | 405,192,560,110 |
| (4) Other Unfunded Liabilities (Note 6) | 205,834 | 119,234 |
| e. Total Unfunded Liabilities | <u>\$411,891,886,938</u> | <u>405,192,679,344</u> |
| 6. TOTAL LIABILITIES | \$517,996,351,011 | 498,928,162,137 |
| NET POSITION | | |
| 7. Fund Balances: | | |
| a. Revolving Fund Balances | | |
| b. Trust Fund Balances (Note 7) | | |
| c. Appropriated Fund Balances | | |
| d. Total Fund Balances | | |
| 8. Less Future Funding Requirements (Note 8) | <u>(\$411,891,886,938)</u> | <u>(\$405,192,679,344)</u> |
| 9. Net Position | <u>(\$411,891,886,938)</u> | <u>(\$405,192,679,344)</u> |
| 10. Total Liabilities and Net Position | \$106,104,464,073 | \$93,735,482,793 |

The accompanying notes are an integral part of these statements.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

Principal Statements 19

Department/Agency: DOD Military Retirement Trust Fund
 Reporting Entity: Principal Statements
 Statement of Operations (and Changes in Net Position)
 for Period Ended September 30, 1992
 (Dollars)

| | 1992 | 1991 |
|--|-------------------------|-------------------------|
| REVENUES AND FINANCING SOURCES | | |
| 1. Appropriations Expensed | | |
| 2. Revenues from Sales of Goods | | |
| a. To the Public | | |
| b. Intragovernmental | | |
| 3. Interest and Penalties, Non-Federal | | |
| 4. Interest, Federal | \$9,374,859,847 | \$8,491,808,035 |
| 5. Taxes | | |
| 6. Other Revenues and Financing Sources (Note 9) | 27,483,155,269 | 27,974,768,279 |
| 7. Less: Taxes and Receipts Returned to the Treasury | | |
| 8. Total Revenues and Financing Sources | <u>\$36,858,015,116</u> | <u>\$36,466,576,314</u> |
| EXPENSES | | |
| 9. Cost of Goods or Services Sold | | |
| a. To the Public | | |
| b. Intragovernmental | | |
| 10. Program or Operation Expenses (Note 10) | 24,557,136,110 | 23,241,017,939 |
| 11. Depreciation | | |
| 12. Bad Debts and Write-offs | | |
| 13. Interest | | |
| a. Federal Financing Bank/Treasury Borrowing | | |
| b. Federal Securities | | |
| c. Other | | |
| 14. Other Expenses | | |
| 15. Total Expenses | <u>\$24,557,136,110</u> | <u>23,241,017,939</u> |
| 16. Excess (Shortage) of revenues and Financing Sources Over Total Expenses Before Adjustments | 12,300,879,006 | 13,225,558,375 |
| 17. Plus (Minus) Adjustments: | | |
| a. Extraordinary Items (Note 11) | 19,000,086,600 | (300,003,079) |
| b. Prior Period Adjustments | | |
| 18. Excess (Shortage) of Revenues and Financing Sources over Total Expenses | (6,699,207,594) | 13,525,561,454 |
| 19. Plus: Unfunded Expenses | 19,000,086,600 | (300,003,079) |
| 20. Excess (Shortage) of Revenues and Financing Sources Over Funded Expenses | 12,300,879,006 | 13,225,558,375 |

The accompanying notes are an integral part of these statements.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

20 Principal Statements

Department/Agency: DOD Military Retirement Trust Fund
Reporting Entity: Principal Statements
Statement of Operations (and Changes in Net Position)
for Period Ended September 30, 1992
(Dollars)

| EXPENSES Continued | 1992 | 1991 |
|--|----------------------------|----------------------------|
| 21. Net Position, Beginning Balance | (\$405,192,679,344) | (\$418,718,240,798) |
| 22. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses | (6,699,207,594) | 13,525,561,454 |
| 23. Plus (Minus) Equity Transfers | | |
| 24. Net Position, Ending Balance | <u>(\$411,891,886,938)</u> | <u>(\$405,192,679,344)</u> |

The accompanying notes are an integral part of these statements.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

Principal Statements 21

Department/Agency: DOD Military Retirement Trust Fund
Reporting Entity: Principal Statements
Statement of Cash Flows (Indirect)
for the Period Ended September 30, 1992
(Dollars)

| | 1992 | 1991 |
|---|---------------------------|---------------------------|
| Cash Flows from Operating Activities: | | |
| 1. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses | (\$6,699,207,594) | \$13,525,561,454 |
| Adjustments affecting Cash Flow: | | |
| 2. Appropriations Expensed | | |
| 3. Decrease (Increase) in Accounts Receivable | (411,802,348) | (450,738,730) |
| 4. Decrease (Increase) in Loans Receivable | | |
| 5. Decrease (Increase) in Other Assets | | |
| 6. Increase (Decrease) in Accounts Payable | 68,102,274 | 151,701,933 |
| 7. Increase (Decrease) in Debt | | |
| 8. Increase (Decrease) in Other Liabilities | 19,000,086,600 | (300,003,079) |
| 9. Depreciation and Amortization | | |
| 10. Other Unfunded Expenses | | |
| 11. Other Adjustments | | |
| 12. Total Adjustments | <u>18,656,386,526</u> | <u>(599,039,876)</u> |
| 13. Net Cash Provided (Used) by Operating Activities | <u>\$11,957,178,932</u> | <u>\$12,926,521,578</u> |
| Cash Flows from Non-Operating Activities: | | |
| 14. Proceeds from Sales of Investments | (11,942,270,423) | (12,937,034,656) |
| 15. Proceeds from Sales of Property, Plant and Equipment | | |
| 16. Purchases of Investments | | |
| 17. Purchases of Property, Plant and Equipment | | |
| 18. Net Cash Provided (Used) by Non-Operating Activities | <u>(\$11,942,270,423)</u> | <u>(\$12,937,034,656)</u> |
| CASH PROVIDED (USED) BY FINANCIAL ACTIVITIES | | |
| 19. Appropriations (Current Warrants) | | |
| 20. Add: | | |
| a. Restorations | | |
| b. Transfers of Cash from Others | | |
| 21. Deduct: | | |
| a. Withdrawals | | |
| b. Transfers of Cash to Others | | |

The accompanying notes are an integral part of these statements.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

22 Principal Statements

Department/Agency: DOD Military Retirement Trust Fund
Reporting Entity: Principal Statements
Statement of Cash Flows (Indirect)
for the Period Ended September 30, 1992
(Dollars)

CASH PROVIDED (USED) BY FINANCIAL ACTIVITIES

| Continued | 1992 | 1991 |
|---|---------------------|-----------------|
| 23. Borrowing from the Public | | |
| 24. Repayments on Loans | | |
| 25. Borrowing from the Treasury and the Federal Financing Bank | | |
| 26. Repayments on Loans from the Treasury and the Federal Financing Bank | | |
| 27. Other Borrowings and Repayments | | |
| 28. Net Cash Provided (Used) by Financing Activities | | |
| 29. Net Cash Provided (Used) by Operating, Non-Operating and Financing Activities | 14,908,509 | (10,513,078) |
| 30. Fund Balance with Treasury, Cash, and Foreign Currency, Beginning | 28,256 | 10,541,334 |
| 31. Fund Balance with Treasury, Cash, and Foreign Currency, Ending | <u>\$14,936,765</u> | <u>\$28,256</u> |

The accompanying notes are an integral part of these statements.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

Principal Statements 23

Department/Agency: DOD Military Retirement Trust Fund
 Reporting Entity: Principal Statements
 Statement of Budget and Actual Expenses
 for the Period Ended September 30, 1992
 (Dollars)

| Program Name (s) | BUDGET | | | ACTUAL |
|---------------------|--------------------------|-------------------------|------------|-------------------------|
| | Resources | Obligations | | Expenses |
| | | Direct | Reimbursed | |
| Military Retirement | \$124,927,039,796 | \$24,578,213,476 | | \$24,557,136,110 |
| Totals | <u>\$124,927,039,796</u> | <u>\$24,578,213,476</u> | <u></u> | <u>\$24,557,136,110</u> |

Budget Reconciliation

| | |
|-------------------------------------|-----------------------------|
| A. Total Expenses | \$24,557,136,110 |
| B. Add: | |
| (1) Capital Acquisitions | |
| (2) Loans Disbursed | |
| (3) Other Expended Budget Authority | |
| C. Less: | |
| (1) Depreciation and Amortization | |
| (2) Unfunded Annual Leave Expense | |
| (3) Other Unfunded Expenses | <u> </u> |
| D. Expended Appropriations | |
| E. Less Reimbursements | |
| F. Expended Appropriations, Direct | <u>\$24,557,136,110</u> |

The accompanying notes are an integral part of these statements.

***DOD MILITARY
RETIREMENT TRUST
FUND***

FOOTNOTES

DoD Military Retirement Trust Fund Financial Statements for FY 1992

Footnotes 27

NOTES TO THE PRINCIPAL STATEMENTS DOD MILITARY RETIREMENT TRUST FUND SEPTEMBER 30, 1992

Note 1 Significant Accounting Policies:

The DoD Military Retirement Fund was authorized in PL98-94 for the accumulation of funds in order to finance on an actuarially sound basis liabilities of the Department of Defense under military retirement and survivor benefit programs. The accounting is accomplished by the Defense Finance and Accounting Service - Defense Accounting Office - Arlington. These financial statements are presented on the accrual basis of accounting as required by Title 2, "Accounting Principles and Standards" published by GAO and the DoD Accounting Manual. Reports are prepared from Trial Balance data generated by an automated system which is on the accrual basis. Balances are reconciled monthly with U.S. Treasury records.

The program is funded by:

- (1) Annual unfunded liability payment from Treasury.
- (2) Monthly Service contributions as a percentage of base pay.
- (3) Interest on investments.

Note 2 Fund Balances with Treasury:

| | |
|-------------|--------------|
| Trust Funds | \$14,936,765 |
|-------------|--------------|

Note 3 Investments:

| | (1) Face Amount | (2) Market Value | (3) Amortization Method | (4) Unamortized Premium/ (Discount) | (5) Investment Net (Book Value) |
|-----------------------|-----------------------|------------------------|-------------------------------|--|--|
| B. Federal Securities | | | | | |
| Non-Marketable | \$87,753,439,000 | \$122,147,021,564 | Effective Int | \$14,610,838,220 | \$102,364,277,220 |

Note 4 Other Funded Liabilities, Non-Federal:

Assets available for benefits. See Note 5 below.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

28 Footnotes

Note 5 Pensions and Other Actuarial Liabilities:

| | (1) Actuarial Present Value of Projected Plan Benefits | (2) Assumed Interest Rate(%) | (3) Assets Available to Pay Benefits (Net Assets) | (4) Unfund Actuarial Liability |
|---------------------------|---|------------------------------------|---|--------------------------------------|
| Major Program Activity | | | | |
| Pension Plan | \$515,900,000,000 | 7.5% | \$104,008,318,896 | \$411,891,681,104 |

Other Information: The Military Retirement System is an single-employer plan. It is a defined benefit plan. Administrative costs are not borne by the plan. The Trust Fund uses an aggregate entry-age normal cost funding the actuarial cost method used is the aggregate entry-age-normal. Projected revenues, as authorized by PL98-84, are to be paid into the Fund at the beginning of each fiscal year by the Secretary of the Treasury as certified by the Secretary of Defense. This permanent indefinite appropriation, determined by the Board of Actuaries, represents the unfunded liability for service performed prior to October 1, 1984.

Note 6 Other Unfunded Liabilities:

| | |
|---------------------------|-----------|
| Death Payment Contingency | \$205,834 |
|---------------------------|-----------|

Note 7 Trust Fund Balances:

Cumulative Results of Operations (Trust Funds)

Reported as zero. Cumulative results of operations are reported as funded liabilities.

Note 8 Future Funding Requirements:

| | |
|-------------------------------|--------------------------|
| | 1992 |
| A. Actuarial Liabilities | \$411,891,681,104 |
| B. Non-Actuarial Liabilities: | |
| (1) Death Payment Contingency | 205,834 |
| Total | <u>\$411,891,886,938</u> |

Public Law 98-94 required that the military retirement system be funded. The DoD is responsible for the monthly normal cost payments and the Treasury for payments on the Unfunded liability.

DoD Military Retirement Trust Fund Financial Statements for FY 1992

Footnotes 29

Note 9 Other Revenues and Financing Sources:

| | 1992 |
|--|-------------------------|
| (1) Normal Cost Contributions form Services | \$16,314,155,269 |
| (2) Unfunded Liability Payment form Treasury | 11,169,000,000 |
| (3) Transfer from OPM-CMA Judges | |
| Total | <u>\$27,483,155,269</u> |

Note 10 Program or Operating Expenses:

A. Operating Expenses by Object Classification:

| | 1992 |
|----------------------------------|------------------|
| Insurance Claims and Indemnities | \$24,557,136,110 |

Note 11 Extraordinary Items:

| | 1992 |
|--|---------------------------|
| (1) Changes in Actuarial Liability | (\$19,000,000,000) |
| (2) Changes in Death Payment Contingency | (86,600) |
| Total | <u>(\$19,000,086,600)</u> |

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Part VI - Management Comments

Assistant Secretary of Defense for Force Management and Personnel Comments



FORCE MANAGEMENT
AND PERSONNEL

THE OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D C 20301-4000

28 MAY 1993

MEMORANDUM FOR DEPUTY ASSISTANT INSPECTOR GENERAL FOR ANALYSIS &
FOLLOWUP

SUBJECT: DoD Inspector General's Report on the Military
Retirement Trust Fund financial statements for FY 1992
(Project No. 2FH-2014)

Force Management & Personnel (FM&P) has no comments this
report.

A handwritten signature in cursive script, reading "Jeanne B. Fites".

Jeanne B. Fites
Acting Deputy Assistant Secretary
(Requirements and Resources)

Audit Team Members

| | |
|--------------------|--------------------------------|
| Nancy L. Hendricks | Director, Financial Management |
| Raymond D. Kidd | Program Director |
| John M. Seeba | Project Manager |
| Virginia A. Bonds | Team Leader |
| Linda F. Jones | Team Leader |
| Judy K. Palmer | Auditor |
| Mary E. Vitale | Auditor |
| Kristin L. Takac | Auditor |
| Susanne B. Allen | Editor |

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